Queen's University

Course in Banking

LESSONS X-XI

Economics

LESSON X.

The Distribution of Wealth.

Meaning of the term.

It is customary to divide the field of Economics into four sections, dealing respectively with the production, the exchange, the distribution, and the consumption of wealth. This division is made merely for convenience in treatment, and does not imply that it is possible to discuss any aspect of the industrial system without bearing constantly in mind the other aspects. The next few lessons will deal with the third of these fields, the Distribution of Wealth.

This term is used in two senses. It means, first, the process by which the wealth produced by joint action is divided among the several claimants. This is a problem of peculiar difficulty and importance in our time. Under conditions such as existed in England during the Home period (Lesson I), when each community and each household was almost entirely self-sufficient, the question of distribution was a simple one. Each household consumed most of what it produced and produced most of what it consumed: there were few joint products to be shared. Again, under a system of communism such as Cabet favoured, the problem would be equally simple. There would in this case be many products in whose making scores or hundreds might have shared, but the Gordian knot would be cut by the adoption of the simple rule that everybody should be given an equal or identical share of the total product of the community. Such a society would doubtless face practical problems of great if not insoluble difficulty, but the distribution problem would in theory be very simple.

Under actual conditions, however, the process of distribution is a very complex one. The division of labour has been carried very far; the co-operation of hundreds or of thousands is required to produce a single commodity; few men, except farmers, produce more than a small fraction of what they consume, and may in fact consume nothing of what they themselves share in producing. Here is a great factory which every day turns out fifty thousand yards of cloth: what determines how much of this product, or of the money for which it will sell, is to go to the landlord on whose land the mill is built, how much to the far-off bondholder, or to the shareholder who may or may not attend an occasional annual meeting, how much to the managing director, to this superintendent or that salesman, this girl at the loom, this man in the dye-house, to the engineer in the power-plant or the bookkeeper in the office? Or, if we

classify all the shares of these various claimants under the heads of wages, interest, rent, and profit, what are the laws which determine the amount of each of these shares? This is the problem which the student of economics attempts to solve when dealing with the distribution of wealth as a *process*, or from the *functional* point of view, that is, considering the share which falls to each of the claimants according to the part or function played in the great co-operative task of modern production.

In the second sense, a discussion of the distribution of wealth has to do with *results* rather than with *processes*, with *personal* rather than with *functional* distribution. The same man may be in receipt of interest on a bond he holds, rent from a house in which he has invested, and wages or salary for his own services. To cover the whole field of distribution, therefore, it is necessary to look at it from the side of the receipt of income as well as from the side of its origin. What, we may ask, are the facts as to the manner in which wealth, however, derived, is shared among men to-day? What are the facts as to equality or inequality? Is the gap between rich and poor widening or lessening? What are the causes of inequality? Is it desirable, is it alterable? These are some of the questions which present themselves under the head of "the distribution of wealth" in the second sense.

This second question, which can be covered more briefly, will be dealt with in the present lesson, while distribution of wealth as a process will be considered in the following lessons.

> *The distribution of wealth is the most debated topic in economic theory and the centre of interest in economic practice. In our modern days millions of men co-operate in a vast, intricate system for the production of wealth. What shares of this joint product do they secure as reward?*

The Distribution of Property and Income.

No phase of Economics has been so much discussed as this question of the equality or inequality, the fairness or the injustice, of the sharing of material wealth to-day. It is preeminently *the* social question. Yet neither the socialist who denounces the present system, nor the conservative who defends it, has been able to state precisely what are the facts thus denounced or defended. It is difficult to obtain precise statistics as to wealth or poverty. In those countries which have a fully developed system of income and inheritance taxes, notably the United Kingdom and several of the German states, fairly exact conclusions may be reached, but in other countries

recourse must be had to indirect means of estimating the division, or to general observation.

In the United Kingdom, where incomes below £160 are exempt from taxation, the facts as to *income*, in 1904, are thus condensed by Bowley and Taussig:

The number of families with incomes under £160 was	6,775,000
The number of incomes between £160 and £700 was	830,000
The number of incomes between £700 and £2000 was	122,000
The number of incomes between £2000 and £5000 was	32,400
The number of incomes between £5000 and £50,000 was	14,200
The number of incomes over £50,000 was	350

That is, in a population of 43,000,000, some 5,000,000 belong to families with an income of £160 or more, and these people receive half the total income of the nation; the remaining 38,000,000, those below the income tax level, share the other half.

The facts as to *property* in the United Kingdom of course show greater inequality. Chiozza-Money points out that, on the average of the years 1899-1904, and drawing the line between rich and poor as high as £1000, of the 714,000 persons who die every year, 7,459 of the rich leave £257,000,000, while 686,541 of the poor leave between them only £29,600,000. "On an average eight millionaires die leaving between them three times as much wealth as is left by 644,000 poor persons who die in one year. Again, in a single year, the wealth left by the few rich people who die approaches in amount the aggregate property possessed by the whole of the living poor."

For Prussia, the following estimate, based on an income tax which exempts 900 marks ($225), is drawn up by Schmoller:

4,500,000 families have incomes of 900 marks or less, averaging, say, 650 marks.

2,500,000 families have incomes of 900 to 3000 marks, average 1350.

400,000 families have incomes of 3000 to 100,000 marks, average, 10,000.

As to *property*, only one out of seven families in Prussia possesses more than 6000 marks.

In other countries, the inequality is less extreme. In France, for example, the greater relative importance of agriculture, the laws requiring fairly even distribution of property among definite heirs, and the widely diffused practice of thrift, have resulted in more even distribution of wealth and more uniform prosperity.

In the Unted States the hugeness of the fortunes which have been accumulated by a few men and the wide distribution

of farm and other property among the masses of the people are alike striking, but, until the new federal income tax is extended and its results analysed, exact information will continue to be difficult to otbain. According to the report issued by the Secretary of the Treasury, in 1913-14, the first year in which the tax was imposed, the statistics so far as ascertained were as follows:

Incomes Reported	Persons Taxed in United States	Persons Taxed in New York City
$1,000,000 or more	44	
$500,000 to $1,000,000	91	82
$400,000 to $500,000	44	17
300,000 to 400,000	84	48
250,000 to 300,000	94	46
200,000 to 250,000	145	63
150,000 to 200,000	311	105
100,000 to 150,000	785	278
75,000 to 100,000	998	467
50,000 to 75,000	2,618	879
40,000 to 50,000	2,427	851
30,000 to 40,000	4,553	1,432
25,000 to 30,000	4,164	1,254
20,000 to 25,000	6,817	1,922
15,000 to 20,000	11,977	4,411
10,000 to 15,000	26,818	6,762
5,000 to 10,000	101,718	24,438
3,333 to 5,000	114,448	25,214
2,500 to 3,333	79,426	15,924
Total	357,598	81,982

In Canada, the width and freshness of a half-continent's opportunities, the fortunate selection of racial stocks, the policy of disposing of land to settlers free or at a nominal price, have hitherto tended to prevent great extremes either of wealth or of poverty, but recently the expansion of our financial and industrial machinery and the rapid exploitation of our natural resources, have made it possible to heap up some great fortunes, while the incoming of peoples of lower standards of living, from continental Europe and elsewhere, has brought the problems of poverty closer.

In all old lands the inequalities in wealth are striking and involve serious social problems. Our newer land has been fortunate hitherto in escaping great and permanent inequality, but changing conditions threaten to develop here the dangers both of poverty and of plutocracy.

Present Tendencies.

Is it true, as is so often stated, that the rich are growing richer and the poor poorer? Is the gap widening or lessening? Here again exact data are scarce. We know that the lot of the working classes is better today in practically every industrial country than it was a century ago, that wages are higher, hours shorter, sickness less and life longer, and the provision of free services by the state constantly increasing. By analzing the statistics of the consumption of the articles in widest use, Griffen has shown clearly the improvement in conditions in the United Kingdom, while Bowley presents the following brief summary of the movements of wages in the same country since 1830, (taking the wages paid in 1900 as par, and considering only changes in real wages, that is, not money but the goods that money at each time could buy; since 1900 the cost of living has risen as fast as wages):

Year.......	1830	1840	1850	1860	1870	1880	1890	1900
Real Wages..	45	50	55	60	70	70	84	100

Mallock ponts out that if, in 1800, the whole income of Great Britain had been equally divided among all its people, each person would have received £16, 14s.; whereas, by 1850 the average income per head of the poorer classes (those below the income tax level) was £15 and by 1888 £25: that is, what in 1800 would have seemed a wild communistic dream had by 1888 been more than realized. Again, in 1850 equal sharing would have brought each person an income of £23, 6s.; actually, in 1905, the average income per head of the classes dependent on incomes not exceeding £150, was £29. There are still great swamps of human misery to be drained, still tens of millions in the industrial countries who are without the minimum of possessions needed for bare subsistence and common decency, but slowly, perhaps, and unevenly, but still surely progress is being made.

It is, however, not enough to consider whether the lot of the poorer classes today is better or worse than that of their grandfathers. If growing better, has it been growing better as fast as the fortunes of the rich have grown? Here reliable statistics are still more difficult to obtain. We may take as representative, however, Bowley's conclusion that "if we compare the period 1898-1902 with 1883-1887, it appears that the total income of the people of the United Kingdom has increased not less than 38 per cent., the population about 15 per cent., and the average income per head not less than 20 per cent. . The part of the national income received as wages has increas-

ed 50 per cent. in total or 30 per cent. per wage earner; the part liable to income tax has increased from 35 to 40 per cent. relatively to the population." Or if we accept Baxter's computation for 1867 and Chiozza-Money's for 1907, we find that the manual workers of the same country received almost exactly the same proportion of the total national income, allowing for changes in numbers, at both periods. At worst, then, society is marking time.

How, then, can we explain the undoubted fact that discontent has grown, that both among the Haves and the Have Nots there is a keener sense than ever before of the injustice of many phases of the industrial system? The gap may be no wider, but it is more observed, more keenly felt.

Not least important among the causes of this discontent, so far as the Have Nots are concerned, is the very betterment of conditions. Spenser has called attention to the curious paradox that frequently "the more things improve the louder become exclamations about their badness." When women bore the heavy burdens and received what food was left after their lords and masters had eaten, there was little outcry as to the rights of women; today, when they have secured all but equal privileges, their grievances are proclaimed from the housetops. A century ago, when drunkenness was widely prevalent, when in poorer quarters "drunk for a penny, dead drunk for two-pence, and clean straw for three-pence" was a possibility, and when the man of higher rank who could not take his bottle or two of wine was held a milksop, and judges on the bench and premiers in parliament came half drunk to their duty, there was little agitation against the evils of drink; but today, when more exacting industrial demands and temperance agitation have produced comparative sobriety, the prohibition movement sweeps whole states. So with the condition of the average working man of today as compared with that of his ancestors. The improvements have simply whetted the appetite for more, nourished the spirit of resistance. The hopelessness of utter poverty and ignorance crushes; a half advance rouses fiercer demand and stronger power of insistence.

At the same time that ambition is stirred, the goal tantalizingly recedes into the distance. The higher pedestal opens new horizons. The standard of living rises faster than the means at our command. Your standard of comparison is set, not by your outgrown self, nor by your ancestor dead and gone, but by the more fortunate about you. The optimist may remind you that one born in your station of life a century ago, or in that poorer land from which you emigrated, would have thanked God humbly for meat once a week; that not very long ago cotton was a luxury forbidden by law to women below the rank of countess, or that Plantagenet kings slept on rushes

and dined by the light of a tallow dip. To no purpose: it matters little that your great-grandfather walked shoeless, while you walk shod; it matters much that you walk, while your neighbor whizzes by in his ninety-horse-power car or casts upon you the shadow of his aeroplane. The luxuries of yesterday becomes today's necessities. "What possible uneasiness was it to the workingman, before the discovery of America, that there was no tobacco to be had? or before the era of printing, that no desirable book could be got?" (Lassalle). More and more, home services and preparations are replaced by the tempting but expensive convenience of the open market.

Democracy sharpens the sting of economic inequality. Equal votes suggest equal purses. When men are born and work and die within the same caste, and are trained to pray Providence to keep them in their proper stations and bless the squire and his relations, it is only the few hardiest spirits who dream of questioning the justice of their lot. But when the barriers of caste are down, and democratic theory teaches that every man is as good as his neighbor, the case is altered.

Religious ties, which formerly enforced content, have weakened. The massing of men in great cities makes agitation easier. When Christianity was a new and revolutionary gospel, it made its appeal to the city proletarian, or poorer workers, not to the "pagans,"—that is, **pagani** or country-dwellers. The new mobility of labour, the rise of a popular press, tend in the same direction: the fierce yellow light that beats upon the multi-millionaire keeps the sins of wealth ever before us.

> *So far as the objective facts go, it seems clear that in most industrial countries the gap between rich and poor is not widening, and that in wages, hours, surroundings and educational opportunities, the lot of the workman is better to-day than it was a century ago. Yet with this betterment, partly, indeed, because of it, there has grown a keener realization of the inequalities that remain. Discontent has followed progress.*

The Causes of Inequality.

In part, inequality of wealth is due to inequality in the ability or character of different men. There is no doubt that initiative, audacity, persistence, thrift, count in the struggle. It is unfortunately not true that superiority in moral qualities alone gives pre-eminence: it may be a more callous disregard of workmen's needs, a more ingenious skill in avoiding the law, a lack of interest in anything but money-making, that makes the difference between success and failure. But whether the

qualities are moral or immoral—and any society that hangs together, that builds up an elaborate system of credit, that is, of confidence, must be fundamentally honest—there is a great variation in the degrees in which men possess them. Even were absolute equality established tomorrow, it would soon disappear because of differences in thrift, ability, energy, luck and sharp practice.

But it is not merely original differences that count. Inequality tends to perpetuate itself. By our system of inheritance some men begin the race of life at scratch, while others have a big handicap to overcome. "The curse of the poor is their poverty and the opportunity of the wealthy is their wealth," or, as was said long ago, "To him that hath shall be given, and from him that hath not shall be taken even that which he hath." It is not merely the possession of property from which interest or rent may be drawn that makes the difference: the possession of wealth usually means also a better training, a knowledge of opportunities, and friends in high places. It may be, indeed, that wealth will bring temptation and luxury breed feebleness, just as poverty may stimulate thrift and ambition. An old American proverb ran, "From shirt-sleeves to shirt-sleeves in three generations." Fortunes do not go on increasing indefinitely: a single dollar at four per cent. compound interest would amount in a century to $50, in four centuries to $6,000,000, in a thousand years to 100 quadrillion dollars, and in two thousand years—little more than the Christian era—to 100 quadrillion times 100 quadrillions or many times the value of a world of solid gold. In less than seven centuries it would amount to several times the total capital of North and South America. Evidently fortunes are in time divided or come to a standstill. Yet with all allowance made, the advantage of the start given by the inheritance of wealth, and the part it plays in maintaining or increasing inequality are undeniable.

> Inequality ~~The quality~~ *is due in part to unequal capacities and in part to unequal starts. While inheritances are not always blessings, and while there is a limit to the power of fortunes to accumulate, an increasing measure of the inequalities in wealth which exist appears to be due to inherited advantages.*

Is Inequality Defensible?

Is a system which produces such great inequalities of wealth desirable? This is a complex and far-reaching question; some of the more important aspects may be indicated briefly.

Is it fair? the question may be put. Do the inequalities which exist correspond to differences either in individual merit displayed or in social benefits conferred? It is said they do not, on several grounds. First, that wealth is often gained by unsocial practices, by activities that injure rather than help one's fellows. The little grafter with his thirty-five inch yard-measure or his sand in the sugar, the wholesale grafter with his swindling stock-selling scheme, may grow rich at honest men's expense. Doubtless so; such instances are only too common. But, as suggested in a previous paragraph, no enduring commercial structure can be built on fraud; it is the sound honesty of the majority that provides the drab background for the scarlet sins; unless there existed a general expectation of squareness, based on experience, the operations of the crook would be impossible.

Second, it may be said that even where men are engaged in socially useful work, and are more able and more diligent than their fellows, the reward they receive is out of all proportion to the degree of superiority of their abilities. Here, again, there is much force in the statement. Nothing succeeds like success; the man who stands out above the ruck ever so little will forge ahead much farther than the difference in capacity would seem to warrant. The top rungs are less crowded and once the crowd is passed progress is much less impeded. However, it may be possible, as will be suggested later, by increasing, on the one hand, the freedom of opportunity, and, on the other, by taxation of great fortunes, to lessen somewhat this disproportion without withdrawing the necessary stimulus of some very great prizes.

Third, the individual may be said to owe to society much of his success: without the training he has received, without the civilization, the arts, the mechanism of trade, which has been painfully and slowly built up by countless generations of forgotten workers, without the markets his fellows provide, the abilities of the ablest man would have found little scope. True, and this fact is one justification for substantial taxation of great fortunes; still, it is to be remembered that this social heritage and this social opportunity exist—or should be made to exist—for all men alike, and do not of themselves prove that one man who made better use of these advantages than his fellows has been unduly rewarded. Finally, it may be argued that so far at least as inequality results from inheritance it does not correspond to any individual merit on the part of the present possessor. This has more validity, but it involves an examination of another aspect of the question, namely, the social advantages, or otherwise, secured by the inequality itself. For institutions must be judged not merely by origins but by results, by the way they work out.

Broadly speaking, differences in success in wealth-making appear to correspond to real differences in capacity and, in less degree, to real differences in the services rendered society. It must be the aim to make this still more true by increasing the opportunities of the average man and by restricting the unsocial activities by which wealth is unfairly gained.

Inequality, in the degree attained in most industrial countries, means at one extreme a "submerged tenth," a class of people lacking the bare necessities, degraded and shut out from the realization of their human possibilities, and at the other extreme a class beyond the need of working at all to secure all the material advantages life can offer. If the "submerged tenth" were an inevitable product of our present industrial system, and peculiar to this system, their lot would constitute a very strong argument indeed for a charge to, say, some socialistic or communistic system. But it may be pointed out that even within the framework of our present society it is possible to reduce the numbers and the suffering of this minority, and that under any other system it is conceivable that there would, instead, be a "submerged half." And what of the "emerged tenth," the leisure class? Here the question turns first upon the fact whether or not this class give services to society which we could not otherwise secure, and thus directly justifies its existence, "pays for its keep." It has often been pointed out that it is to a leisure class, to men who were not tied down to sordid cares, not hampered by selfish fears and strivings, that the world owes much of its progress. Arts, science, literature, political progress, everything that constitutes civilization, is said to be largely a leisure class creation. The old Greek thinkers made the possession of leisure the indispensable condition of citizenship. The Athenians who gave the world some of its most imperishable treasures alike in art and in science and in political development, the Romans who gave law and discipline, both reared their civilization on a foundation of leisure-permitting slavery. English politics in the past has largely been carried on by a wealthy leisure class. To these claims it might be responded that for one man who uses his leisure wisely, in the service of his fellows, ten may use it in selfish pleasure; that no class can long be trusted to look after the interests of other classes; that art or literature divorced from the hard realities of life tends to become frivolous and pedantic; that it is in the day's work and by the men who are in the thick of the struggle that the most important practical improvements are hammered out; and that a society in which all shared both work and leisure would fare better

than one in which specialization was carried to the extreme of giving one class no set work and another no possible leisure. It may be said, then, that while it is possible that much social service will be rendered by a leisure class, it does not appear that this is the only way such services may be secured, or that these services in themselves are sufficiently great and certain to justify society paying for them in advance, as it were.

If, then, the existence of a leisure class, and especially the institution of inheritance on which it is built up, are to be justified, it must be on other grounds—notably, on the ground that these institutions are part of the price we pay for the efficiency of our system of private property. Whether or not wholly desirable in themselves, it may be that they are defensible as necessary incidents, as an essential part, of this system. Is the system, then, of private property itself justifiable, or would it be better to set up common or state ownership and control of all revenue-producing property? There is no heaven-born sanction for private property. Like all other social customs and institutions it can be justified, and will endure, only if it proves the most efficient method of carrying on society's work, of meeting human needs. Judged by this test, private property, with all its faults, has been justified by long centuries of experience. This experience has shown that, day in and day out, the average man will not labour steadily and effectively unless there is some direct connection between his effort and the welfare of himself or family. Men will throw uncounted energy into a sport or a hobby; a fortunate few find their day's work of absorbing interest; in times of crisis many will give life itself for their fellows. But in the daily round of routine toil, with no drums beating, no hobby-interest leading on, we find that the spur of necessity, the lure of future leisure, the desire for the power of wealth gives, or the desire to safeguard the future of one's family, are needed to keep us to the mark. By throwing on each man the main responsibility for his own welfare, we ensure much greater activity and thrift and enterprise (not always, but prevailingly, turned in helpful directions) than if each of us could rely on the government or on the community for support, and if our individual fortunes had only a very remote connection with our individual efforts. So much more effective is this means of organizing production, with all its wastes, with all its unfairnesses, that it may well be maintained that the unequal share which the poorer man obtains under such a system is larger than would be his equal share of the product of a socialistic community. Part and parcel of this system, is the institution of inheritance. Undoubtedly one of the chief springs of activity is the desire to provide for the future of one's family. On this ground, then, inheritance may be defended, for the effect it has on the man

who bequeathes the estate more perhaps than for the effect it has on the man who receives it.

> *A leisure class, a class placed by inheritance beyond the need of toil, has been paid in advance for the work it is to render society in art or politics or social endeavor. Whether it usually performs the services for which it is thus paid is open to grave doubt. The institution of inheritance is to be defended rather on the ground of the stimulus it affords the man who built up the fortune. It seems an effective, if not an essential, feature of the system of private property to which, with all its faults, industrial progress is mainly due.*

Remedy of Defects.

While, however, it seems that, on the whole, the system of private property and inheritance works out to the advantage of the community, we must not shut our eyes to its serious defects. It works well if opportunity is equal, if free scope is given for the development of capacity, but in so far as opportunity is restricted, as some men are shut out from the training necessary to run the race, or others are permitted to use unfair means in the contest, the ideal results pointed to by the defenders of private property cannot be expected. We must of course remember that given men and women as they actually are to work with, no system of organizing industrial effort can work perfectly; and, in fact, if we did succeed in attaining our ideals, that would mean stagnation, not perfection, would mean that men had ceased to dream and to plan and to strive for ever better ends. Yet it should be possible to make the fact of to-morrow at least approximate somewhat closer to the ideal of to-day.

The aim of those who seek reform rather than revolution, who wish to remove the defects which mar the working of private property while retaining its indispensable strong points, is to open as wide as possible the door of opportunity. If every man can be ensured decent home surroundings by improvements in housing or transportation methods, an adequate cultural and technical education, and protection by the state in those matters which individual or even collective bargaining cannot well effect, such as sanitary regulation of factories or provision for compensation for accidents, and if, further, monopoly privileges are done away with, and financial and commercial fraud guarded against as far as foresight can go, then, with somewhat greater approximation toward a free field and no favour, we can look for more efficient production and

more just distribution. Some of the more important means to this end will be discussed in later lessons.

> *Private property will endure only if we 'lop the mouldering branch away," and secure as far as possible the conditions under which in theory private enterprise and social welfare coincide. We must seek to combine social justice and individual initiative.*

Questions for Review.

1. In what two senses is the term 'distribution of wealth' used?

2. Why does the distribution of wealth present both greater theoretical and greater practical difficulties than in early days?

3. What sources of information are available for the study of the facts as to personal distribution of wealth?

4. What are the essential facts as to equality or inequality in the United Kingdom?

5. Are there any factors in the United Kingdom or Prussia tending to produce or perpetuate inequality of wealth, which are not found in Canada?

6. Why is there greater equality in France than in the United Kingdom?

7. What are the special factors which have made for equality in Canada?

8. What have been the sources of the outstanding fortunes in the United States? in Canada?

9. How far are our problems of poverty problems of immigration?

10. How may tendencies as to distribution of wealth be estimated?

11. What is Mallock's argument as to the share of national wealth possessed by the poorer classes in the United Kingdom now as compared with their share in 1800?

12. In what ways do you think the average English workingman is better off to-day than his grandfather? in what ways worse off?

13. Why, if conditions improve, do discontent and agitation increase?

14. Distinguish between the control of wealth and its ownership.

15. With what justice can the prevalent social and political defects be charged to the industrial system? Does the mere fact that defects exist condemn a system? Would it be desirable to be absolutely satisfied with any system as perfect?

16. In building up the several fortunes which exist in your community, what part do you think has been played by inheritance? by unusual enterprise? by industry? by thrift? by fraud? by luck?

17. Why do not fortunes go on increasing indefinitely?

18. If ability is inherited, why should not wealth be inherited?

19. Are there any restrictions, in Canada, upon the liberty of a testator to do what he likes with his property?

20. Does a leisure class justify its existence by its contributions to culture? Is the setting up of a leisure class the only way such ends can be attained?

21. Do you see any difference between saying that things ought to be so and so and saying that the state should at once proceed to make them so?

22. Which is more important, approximate equality of possessions or approximate equality of opportunity? Is it necessary to destroy the present order to secure the latter?

23. "To pull down those who are superior in wealth, culture, talent, virtue or education is to act like an army invading a hostile country, which should shoot its own advance guard." Comment.

24. What instances occur to you of one-time luxuries which have to-day become necessities to nearly all classes?

Questions for Written Answer.

1. Make a list of what appear to you to be the strongest points of our present system of private property and individual competition.

2. Make a list of its weakest points.

3. What do you think are the most necessary steps to take to secure a real equality, or approximate equality, of opportunity in Canada?

4. Are there any reasons why great fortunes are less likely to be dissipated than in the days when the American proverb, "Three generations from shirt-sleeves to shirt-sleeves," was coined?

5. Do any of the Review questions present difficulty?

LESSON XI.

Distribution of Wealth—by Factors.

1. The Process of Distribution.

It was stated in the preceding lesson that the term distribution of wealth is used in two senses. In the sense in which it has already been discussed, it involves a study of the results of economic activities, of the present facts as to personal distribution, of the equality or inequality of the total incomes or possessions, however derived, enjoyed by the people of any community. In the other meaning, it has reference to the process rather than to the results; under this head the student of economics endeavors to understand the laws or factors or forces which determine what share of the total product of any undertaking or of the whole community falls to this claimant, say, the wage-earner, and what share to that claimant, say, the capitalist. This general topic will be discussed in this and following lessons.

In discussing the broad question of the distributive process, it is necessary to examine some of the more important theories which have been held in the past. In many cases these theories do not now receive assent from careful students, but they still influence the statement and treatment of the problem, they linger in popular discussion, and a reference to them will serve to bring out some essential aspects of the complex question and to contribute something to a more adequate solution.

First, who are the claimants in distribution? What are the shares into which the total product is divided? It is customary to recognize four classes of claimants, and four corresponding shares: the landlord is said to receive *rent,* the capitalist *interest,* the wage-earner *wages,* and the entrepreneur or employer *profit.* These shares in distribution correspond in part to the entrepreneur's outlays or costs of production, and include also the residual share that falls to himself as profit. A farmer or manufacturer rents land for cultivation or for a building site: the outlay for rent is one of his costs of production. Next he borrows money: the outlay for interest on this sum is equally one of his costs of production. He hires workmen, and their wages, from his standpoint, are still a third cost. Whatever is left after meeting these demands is his own profit. Whether this classification is ac-

curate or complete will be discussed later. For the present it is sufficient to note that it has been the basis of both the academic and the popular discussion for many years.

Note also that it is not implied that every person falls into one and one only of these categories. The same man may receive rent as owner of a small farm, interest on a government bond, wages for services performed for an employer, and profits on some scheme engaged in during his spare time. In different countries different combinations will be found. In England, for example, agriculture is usually carried on by three clearly distinct classes, the landlord who provides the land and permanent improvements, the farmer, who supplies working capital, renting the land and hiring the laborers, and the laborers, who have little opportunity of ever becoming more than hired hands. In Canada, on the contrary, the one man usually owns the land, provides part at least of whatever working capital is needed, and does much of the labor himself. Again, in France, where the habit of thrift is widespread, artisans or farmers or clerks possess government bonds or savings accounts to a degree unknown in less fortunate countries. Whatever combinations may be formed, however, the various functions are distinct and the classification noted, whether complete or not, provides a useful starting-point in the investigation.

2. Nineteenth Century English Theories of Distribution.

For the greater part of the nineteenth century, certain famous theories of distribution held the field in England and in other countries where English economists exercised influence. While these doctrines were, if true at all, true only in the peculiar conditions of industrial life in nineteenth century England, they were put forward as if universal and eternal truths. Particularly in popular discussion, they assumed a character of dogmatic certainty which gave them a special title to be considered the orthodox or classical doctrines.

One of the significant features of the distribution theory of this period was the attempt to establish a separate law for each factor, distinct explanations of the amount of the landlord's and of the laborer's and of the capitalist's shares in the product. The Ricardian Law of Rent, the Iron Law or Wage-Fund theories of wages, accounted for the shares respectively of landlord and wage-earner: the remainder fell to the capitalist, the residual claimant.

The Ricardian Doctrine of Rent. Most definite and most widely accepted was the theory of rent put forward by several

writers in the early twenties of the nineteenth century, and preeminently by the English banker and economist, David Ricardo.

Ricardo and his followers began by assuming that land was essentially distinct from the other factors of production, labor and capital, and that its share in distribution was settled by distinct and peculiar forces. Nature and natural resources, man and his labor, and the capital, in the form of money, machinery, raw material, which was the result of union of man's labor and nature's bounty, were clearly separable. Ricardo's theory of rent, moreover, was mainly a theory of the rent of agricultural land, though it was extended to cover urban land.

Rent, in the Ricardian view, was a surplus. That is, on practically every farm in cultivation, after the labor and the capital employed had received the normal return due them, it appeared that there was a surplus left, which fell to the owner —whether or not the owner was a different person from the farmer who actually carried on the work. This was the fact of rent, which the law of rent must explain.

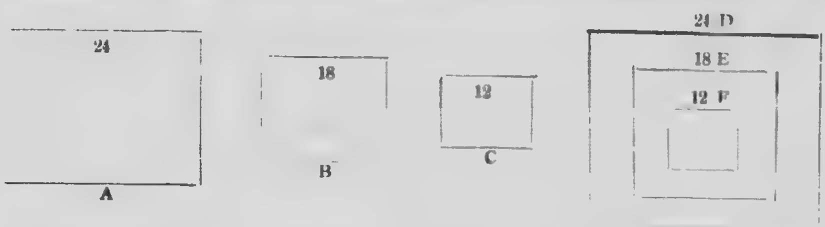
The first step in the explanation was to note the important differences in fertility or accessibility to market between different areas of land, and, further, the differences, so far as any one area was concerned, between the product yielded by the first and by the second and third and later applications of a given amount of labor and capital. It was clear that no two pieces of land were exactly equal, whether in fertility or in situation. It was also clear, and the fact was summed up in the Law of Diminishing Returns, that while every fresh application of labor and capital would increase the total product of a field, yet after a certain point the increase resulting would fall off, would be less than the increase from the previous application. A farmer could go on crowding laborers into his fields, ploughing and reploughing, hoeing and digging, or could double and treble the amount of fertilizer or the extent and variety of machinery used, and with every addition the yield would increase; yet soon or late he would find that the last man or the last hundredweight of fertilizer did not increase the yield as much as previous units of labor or capital had done. When, therefore, population grew and the demand for food grew in proportion, and when it became necessary to utilize less fertile or more remote areas, or to cultivate the old areas more intensively, increasing importance attaching to the differences between the yield under the most favorable conditions and the yield under the least favorable (i.e., at the margin of cultivation, the last land or last land-use found necessary, known as the *extensive* margin of cultivation when the poorest land was referred to, and as the *intensive* margin when the last

and least productive application of a given quantity of labor or capital to a given area was in view).

The second point was that in the same market and for the same staple goods there could be only one price. A bushel of wheat of a certain grade would bring the same return whether grown on fertile or on unfertile land, whether part of a thirty bushel or of a ten bushel to the acre crop. This price must be just sufficient to cover the cost of production, including normal profits, on the poorest land or least profitable land-use necessary to meet the demand for wheat: if not sufficient to meet this cost, this land will not continue to be cultivated; if more than sufficient, still poorer land would be utilized. The value of agricultural products, in short, and of other products subject to the law of Diminishing Return, tends to equal their cost of production on the extensive or intensive margin of cultivation.

Now the cultivator of the richer soil receives the same price per bushel as the man at the margin, and reaps more bushels for the same expenditure of work and capital. He receives a surplus, and this surplus, under free competition, goes to the landlord as Rent. A and B employ the same amount of labor and capital on two rented areas of different fertility. A on the good soil cannot hope to get a higher net reward than B on the poor soil, assuming that B gets enough to pay customary returns on his outlay, interest on his capital and wages for his laborers. For C and D will be glad to take A's land on the same terms as B secures his, paying the landlord the excess above the sum which repays him for his sacrifices in production. The rent of any grade of land, therefore, will just equal the excess of the value of its product over that of the poorest land which is needed to meet the demands of the community. This is Ricardo's law.

A simple illustration may be given. Suppose we have grades of land which can produce respectively, 24, 18, and 12 bushels of wheat, with the expenditure of an equal amount of



capital and labor. At first the demands for wheat may be met entirely by cultivating land A; assume that the price is $1 a bushel, and $24 the return necessary to recompense the labor

and capital employed. Later, population and demand grow; it becomes necessary to use land of grade B. To meet the expenses of production, $24, the wheat produced from this land must bring $1.33⅓ a bushel. But the wheat grown on land A will now bring the same price; twenty-four bushels at the higher price will sell for $32, or enough to pay the usual returns to capital and labor and leave a surplus of $8, which the landlord can exact as rent. If increasing demand makes it necessary to utilize grade C, the price will rise to $2 a bushel, land A will pay $48 — $24=$24 in rent, and land B, $36 — $24 =$12. Similarly, if instead of cultivating new land, more capital and labor are put on the first grade, equal differences in return and consequent equal surplus or rent will develop between applications D, E, and F.

It follows that rent does not affect the price of agricultural products in the least, no matter how great it is. The price of wheat is fixed by its cost of production on the poorest land in use; and on this margin, it has been seen, there is no surplus, no rent is paid; rent, then, does not enter into the expenses of production of that part of wheat which determines price. On the other hand, price determines the rent; price is cause and rent is effect. Demand for more wheat raises its price and makes possible and necessary the cultivation of poorer and poorer soils; the further down cultivation is forced, the larger will be the surplus or rent of the best lands. Thus price determines rent.

Finally, the advocates of this theory recognized that over a period of time improvements in methods of cultivation, in machinery, in transportation, might counteract the tendency to diminishing returns, and help to keep land from rising. They believed, however, that in the race between the growth of population and improvement in methods, the former was likely to win, and was actually winning in the England of the earlier part of the nineteenth century.

The Subsistence Theory of Wages. The share of the landlord having been thus determined, it was necessary to find the law governing the reward of the laborer. The first systematic theory was a simple one, known variously as the Ricardian theory of wages, the Iron Law of wages, or the Subsistence theory. Briefly, it was that the reward of the laborer is determined by the cost of his subsistence or rather the subsistence of himself and family. It is thus expressed by Ricardo:

> The *natural* price of labor is that price which is necessary to enable the laborers, one with another, to subsist and to perpetuate their race, without either increase or diminution. . . . The *market* price of labor is the price which is really paid for it,

> from the natural operation of the proportion of the supply to the demand; labor is dear when it is scarce and cheap when it is plentiful. However much the market price of labor may deviate from its natural price, it has, like commodities, a tendency to conform to it.
>
> It is when the market price of labor exceeds its natural price, that the condition of the laborer is flourishing and happy, that he has it in his power to command a greater proportion of the necessaries and enjoyments of life, and therefore to rear a healthy and numerous family. When, however, by the encouragement which high wages give to the increase of population, the number of laborers is increased, wages again fall to their natural price and indeed from a reaction sometimes fall below it. When the market price of labor is below its natural price, the condition of the laborers is most wretched. It is only after their privations have reduced their number, or the demand for labor has increased, that the market price of labor will rise to its natural price. . . .
>
> It is not to be understood that the natural price of labor, estimated even in food and necessaries, is absolutely fixed and constant. It varies at different times in the same country, and very materially differs in different countries. It depends essentially on the habits and customs of the people.

This theory received support from the actual facts as to wages in industrial England, in the early years of last century: as a matter of fact, they rarely exceeded what was required for bare subsistence. The theory was further strengthened by the observation of the effects of the poor law system. Under this system, allowances werepaid by each parish to the poor, varying with the price of bread and the number in each family. The net result was to relieve employers at the expense of the general taxpayer, by paying for them part of the wages which otherwise they would have had to pay out of their own pockets. As the allowance from the parish went up, wages went down. It seemed hard to explain this fact on any other ground than the subsistence theory of wages. It was found necessary, it may be remarked, to abolish in 1834 this practice of outdoor poor relief, a practice which was demoralizing the laboring classes and threatening to bankrupt the rest of the community.

The Wage-Fund Theory. With the constant improvement in the condition of the laboring classes in England, it became impossible to maintain the subsistence theory in its first form. Consequently more stress was laid on what Ricardo had called market wages as distinct from natural wages. The subsistence level remained as the level to which wages would fall if the poor did not reform their incontinent habits and prevent their numbers from increasing at the rate which so alarmed Malthus

and his followers. But evidently wages might for a long period remain substantially above this gloomy minimum. What determined the range of these fluctuations? Supply and demand, Ricardo had said. But what constituted supply and what demand? The supply evidently was the number of laborers seeking employment, and the demand, went on the Wage-Fund theorists, such as Senior and McCulloch and Mill, consisted of the Wage-Fund, or the capital set aside by employers for the payment of labor. Wages, therefore, equalled the wage-fund divided by the number of laborers.

This theory was not entirely distinct from the subsistence theory, or antagonistic to it. Both theories could be expressed simply as the equation, capital÷number of laborers=average wages. Both rested on a belief in the Malthusian theories of population (see Lesson XIII). The difference lay in that the subsistence theory emphasized the quotient, found it more or less exactly and definitely fixed, determined by the cost of subsistence, while the wage-fund theory emphasized the dividend, found that the exactness, the precision desirable in a law, lay in the funds or goods available for distribution, an amount which could not at any time be suddenly or materially altered. There was a difference also in the applications which could be made of the two theories. The subsistence theory, though developed by orthodox and conservative thinkers, lent itself easily to socialist denunciation. Lassalle, the great German socialist, took it up, styling it the Iron Law of Wages, and claimed that it proved that so long as the present industrial system lasted, there was no hope of betterment for the working class, no hope that wages could permanently exceed the reward of a slave, that is, bare subsistence. The wage-fund theory, on the contrary, opened up indefinite possibilities of progress for the wage-earner, conditioned, however, on his proper behavior. The quotient, wages, could be increased, first, by increasing the dividend; this could be done only by increasing capital, assuming that the proportion of all capital which was set aside for wages remained stationary. The saving habits of the capitalist, therefore, were emphatically in the interest of the wage-earner, and the more capital the employer secured, the better for his men. But it would be vain labor to increase the dividend, the wage-fund, if the divisor, the number of laborers, were to increase as fast, or even faster. The working-classes had it in their own power to determine their fortunes. If they multiplied recklessly, down wages would go; if they showed prudence and foresight and brought up smaller families, wages would rise. If then, wages were low, it was not the capitalist system but the improvident habits of the workingmen which must be held responsible. A further deduction was drawn.

The total wage-fund at any time was a fixed sum. If one body of workingmen, by organizing a trade union, or by any other form of pressure, succeeded in compelling their employer to increase their wages, that simply meant that there was so much the less to divide among their fellows. Advantages gained by the better organized workmen were secured at the expense of other workmen less able or less willing to make such endeavors. It was, therefore, impossible for all workmen to better their lot by trade union effort.

Profits or Interest. The landlord's and the wage-earner's shares being thus determined, it followed that the remainder fell to the capitalist. Clear distinction was not made between the share which fell to him in return for the use of his capital and the share due in return for his direction of the enterprise. In any case, he was the residual claimant. Profits, incidentally, were justified either as the reward of the capitalist's abstinence, in saving his wealth for further production rather than immediately consuming it, or as virtually wages, since capital is merely accumulated labor.

3. Criticism of the Above Theories.

Is Land distinct from Capital? At the outset must be considered the traditional distinction made between land and other forms of capital. In ordinary business usage, the term rent is applied to the payment made for the use of any specific good which must be returned to the owner, whether a farm, a house, a machine or a dress-suit, while interest is taken to mean the return for the use of such a good, when expressed as a proportion of its value, or the return for the use of money or equivalent rights over productive agents. The return for the use of a farm may be expressed either as rent, say, five dollars per acre, or as interest, say six per cent. on the capital value of each acre. Land is thus ordinarily included in capital, and the return for its use is not considered distinct and separate from other shares in distribution. Since Ricardo's day, however, until recent years, many economists have declined to follow popular usage, and have insisted upon treating land as distinct from other forms of capital and drawing up separate laws to explain its share in distribution. The argument for this distinction has been put concisely by Böhm-Bawerk:

> "In many essential respects land and capital take different ways. (1) The former is immovable; the latter, for the most part, movable. (2) The former is a gift of nature; the latter, a result of labor. (3) The former cannot be increased, the latter can be. (4) The landowner has a social and economical position essentially different from that of the capitalist; pro-

perty in land is justified on essentially different grounds from property in movables. (5) Land is the special object of a kind of production which is economically distinguished by many important peculiarities. (6) Income from land, while subject to many laws in common with income from capital, obeys many distinct laws of its own—land rent, for instance, rising with economical development, while interest falls. On all these considerations, it is most convenient to keep land quite distinct from other kinds of productive wealth."

The arguments may be taken up in turn. (1) and (3) Land is not entirely immovable and fixed in supply. So far as area is concerned, it may to a slight extent be lessened, as by the action of wave and tide, or it may be increased, as the Dutch have done in many an acre painfully won from the sea, or as the Chinese have done in carrying countless baskets of earth up mountain sides to form terrace or "bench" lands. And so far as serviceability goes, effectiveness for production, the real quantity of land, the quantity of land-usefulness, may be indefinitely increased by fertilizers, rotation of crops, soil-inoculation and other methods, just as it may be indefinitely lessened by wheat mining, b yreckless exhaustion of the qualities of the soil which alone give it value. Different kinds of land vary in the degree of limitation, just as do different kinds of capital or labor. (2) This point is irrelevant: however originating, the land is here, and the question is, does it differ so greatly in its use or in the laws governing the return for its use as to warrant separate classification? Timber or diamonds may be considered equally gifts of nature. (4) True, and this is of importance in political and ethical discussion, and may afford a basis for distinguishing between land and other forms of capital for purposes of taxation. This difference will be sufficiently considered if under the term capital sub-heads of natural and artificial capital, or earned and unearned wealth, are used for special purposes. (5) This refers to the opinion that the law of diminishing returns applies solely to land. But this is not tenable. This law takes two forms. In the first version it attempts to forecast the future: in the race between the decreasing fertility of the soil and the increasing inventiveness of man, the former was thought bound to win, especially if population kept increasing rapidly and thus made it necessary to utilize ever poorer soils. In this version, the facts of the past half century have shown it is not true; perhaps in the past decade or so demand has been increasing faster than agricultural productivity, but this is partly for other reasons than soil exhaustion. In another version, this law states that here and now, at a given point of time, there is one best adjustment of the factors in production, and that if with a given amount of

land, steadily increasing units of labor and capital are applied, the yield will not increase proportionally. This is true, but it is true of all factors alike; keep the amount of labor stationary, increase the units of land and other capital, and here also the yield will be found not to increase in proportion. (6) This is not a universal rule, nor is it true of land alone, as will be seen later, when any essential factor in production becomes scarce relatively to the others, its share in distribution rises. If land is the scarce factor, its value will increase, but equally so with labor if labor is the factor which is becoming harder to get.

On these various grounds, therefore, it is coming to be agreed by economists that the distinction between land and other forms of capital is not a valid one in this connection at least. It had its origin in the days when the landlords and the manufacturers and financiers in England were distinct classes, with opposing political and social and economic interests,—the days of the anti-corn-laws agitation; while this opposition of interests has not entirely ceased, it no longer has the vital importance it had in Ricardo's and Mill's day, and in any event does not justify, even if it does explain, separate treatment in a theory of distribution.

The Ricardian Law of Rent. One further consideration remains: if the Ricardian theory is correct, the return for the use of the land is so distinct in character, determined by such distinct factors, that on this ground alone, if on no other, land and capital should not be classified together. This theory, however, will not bear examination. It is, in the first place, not a theory of rent, but a theory of differences in rent. The problem of distribution it attempts to answer is, Why does the share that falls, say to the laborer, bear such and such a proportion to the share that falls to the landlord? and its answer does not explain this at all, but simply explains why the share of this landlord bears such and such a proportion to the share of other landlords. Again, it rests on the assumption that there is marginal land in cultivation which pays no rent. Doubtless there is much land that does not pay rent, whether because barren or far from markets, but the moment any piece of land, no matter how barren or remote, becomes necessary for production, its owner will be able to compel the payment of rent for its use. Even for the poorest land in use, and thus affecting supply, there will be some amount of rent, so that rent is not purely a differential. One might, with equal justice, classify machines or laborers in descending order of capacity and by assuming a no-interest machine or no-wages laborer frame a separate and differential theory of interest or wages. This has in fact been done; with what tenability, will be discussed in section 4 below. If sound, the theory of rent

is not peculiar to land alone, nor does it do more than explain differences in rent.

The Subsistence Theory of Wages. Taken literally, this theory clearly does not fit the facts of our time, whatever may have been the case a century ago. Wages are, on the average, much higher than is necessary for mere subsistence. Why is it, if this theory is sound, that wages differ in different trades? Does it require more food to keep an engraver alive than a ditch-digger? Why are wages higher in England than in France? in Canada than in England? to-day than a century ago? Why are the wages of farm laborers higher in summer than in winter? Some of these variations may be explained in Ricardo's way, as being market fluctuations, due to the changes in demand and supply. But if these fluctuations are permanent, if wages rarely, if ever, conform to the subsistence standard, how can this standard be said to be normal, to provide a definite explanation?

Recognizing this failure, some writers in later years have endeavored to reinterpret the theory. The necessaries of life, we are told, must be taken to include not merely the quantity of food necessary to sustain life, the quantity of nitrogen or carbon fuel necessary to keep up steam in the human engine, but the conventional requirements as well, those decencies or comforts which are at any time regarded as being nearly as indispensable as food and shelter themselves. Tobacco, b ythe British workingman, may be considered as much a necessary of life as bread; shoes and stockings, which Adam Smith notes were not in his time worn by the poorer classes in Scotland, are now necessities, not luxuries, to practically every one in that land. A woman may forego a meal to buy a ribbon; and even in the purchase of food regard may be had to conventions, to the use, e.g. of white bread, rather than to food value alone. If that is so, then the iron law becomes a golden law. Wages conform to the standard of comfort of any time, equal what on the whole are considered conventional as well as physiological needs. All that it is necessary to do to better the lot of the working class is to raise their standard of living: wages will keep pace. This is, in fact, an expansion of a qualification made by Ricardo himself: note the last paragraph of the quotation from his treatise.

Unfortunately, while more in keeping with the facts of increasing prosperity than the older version, this new form of theory does not square with realties. Men will lower their standards rather than starve. When hard times come, some of the ground gained in prosperous days is lost again. In part at least, standards of [illegible] are effect, not cause of wages. It is true, however, th[illegible] existence of a definite standard of

habits and conventions may tend to stiffen the resistance of workmen to a proposed cut and to enlist public sympathy on their side. The standard of living is a real factor in determining wages, but it is only one factor, and it operates, as will be noted below, only in so far as it affects bargaining strength.

The Wage-fund theory is also open to serious criticism. Capital, if money-capital or loan-fund is meant, is not at any time a definite and invariable amount; it varies with every change in the credit mechanism, in the relations of debtors and creditors, in the confidence of business men in the future. Nor is any specific proportion of this capital set aside, definitely ear-marked, for the payment of wages, no less, no more; the employer will pay, not a predetermined amount, but what he has to pay or perhaps thinks it decent to pay. If, again, by capital we understand the actual consumption goods available for the support of the laborers engaged in further production, this quantity is less variable, indeed, but in fact the workers in large part produce as they go along the goods out of which their reward is to come, and the amount of these goods varies with their skill and activity. Cotton-mill owners in Lancashire and Bengal may invest the same amounts of capital, but the great difference in the wages of the Lancashire and the Bengalese workmen reflects, among other things, the difference in their productivity. Each new laborer may add more to the product to be shared than the average laborer preceding, and thus increase rather than reduce the wages.

Here, again, however, we must conclude that a theory which so long held the field contained at least a part of truth, if not the whole truth. There may be no fixed wage fund, wages may depend in part on the amount of the future product and not solely on the past savings, but it remains true that there is a close and important relation between the amount of capital and the rate of wages. The principle of demand and supply is sound, but requires to be stated in other terms than those of the wage-fund doctrine.

4. Marginal Productivity Theory of Distribution.

It seems necessary to refer briefly to a later doctrine which has been widely accepted.

A crude productivity theory, in connection with wages, was put forward a generation ago by General Walker, an American economist and keen critic of the wage-fund doctrine. He was led, by his emphasis on the importance of the variations in product in determining wages, to frame a doctrine which, accepting the orthodox Ricardian theory of rent, and developing a special profits theory, went on to declare that the

worker was the residual claimant, and that all increases in the total product would fall to him. This theory, however, which implied that the workman's share came by a process independent of his own bargaining and striving, would be the same whether he demanded much or would be content with little, could not survive criticism.

Since Walker's day, a more elaborate theory has been developed which endeavors to prove that the share in distribution, not only of labor, but of every factor, is exactly equal to its share in the production, or rather to the product of the marginal unit of that factor. The principles of diminishing returns and marginal factors are taken over from the Ricardian doctrine of Rent, and made to apply to all factors. Assume first that labor is the varying factor. The employer adds unit after unit of labor, of the same efficiency, until the point of diminishing returns is reached and passed, until a situation is reached where the increase in product due to the presence of an additional laborer is barely equal to the wage that must be paid. At this point, therefore, the wage paid and the product of the marginal laborer will be equal. And since the last laborer employed is, by hypothesis, of equal efficiency with other laborers, we may widen the conclusion into the statement that the wages of all laborers will tend to equal the marginal productivity of labor. Similarly by assuming in turn that land, capital, managing ability, are the varying factors, we may reach similar conclusions that rent, interest, profits, tend to equal the marginal productivity of the factors to which they correspond.

It is not desirable, in this introductory study of economics, to treat this theory at length, but it is found so widely in current discussion that some points of criticism should be indicated. (1) It assumes a universal condition of diminishing returns. This is not inevitable: if the best adjustment of factors has not been attained (see Section 3), it may be that it is the factor which is deficient that is being increased, with the result that increasing rather than diminishing returns will be found; for example, in American agriculture there is not sufficient labor and capital in proportion to the land occupied, but these factors are increasing, with consequent increasing returns. Again, if the best adjustment has been reached, say in manufacturing, obviously the best course is to increase all the factors at as nearly the same rate as possible, and thus kep the maximum rate of profit, rather than be satisfied with the lower rate attendant on diminishing returns. (2) Not only does the theory assume a condition of diminishing returns, but it assumes that this is true with respect to each of the factors; in other words, the supply of each factor is assumed to be increasing faster than of the others, at the same time—

a rather difficult situation to imagine. (3) The last increment of product is not attributable to the last unit, say of labor, employed in production. It is the product of that unit acting in conjunction with the existing capital, including land. It is as impossible to isolate any part of a joint product and identify it as the contribution of a single factor, as it is to say, when a flash of electricity turns a mixture of oxygen and hydrogen into water, how much of the water is due to the oxygen, how much to the hydrogen, and how much to the flash. (4) It is not clear why the previous laborers should consent to have their wages cut every time a new and less productive laborer was hired. If they did consent, why would it not pay the employer to add laborers even beyond this point? (5) The theory is an excellent example of circular reasoning. It assumes the margin to begin with, a wage-rate for example, which guides the employer in deciding when to stop adding workmen, i.e., when the product of the last man added barely equals this wage. Then it declares that the product at this margin determines wages.

5. THE BARGAINING THEORY OF DISTRIBUTION.

Having thus briefly reviewed some of the more important explanations of the problem of distribution, offered in the past, we may now go on to discuss the theory which at the present time is gaining most acceptance, and which endeavors to combine the partial glimpses of truth offered by each of the previous explanations.

Factors in Production and Claimants in Distribution. The first question that presents itself is, what classification is to be made of the factors in production to which shares in distribution correspond? The accepted classification has been as follows:—

Factors in Production	Corresponding shares in Distribution
Capital	Interest
Land	Rent
Labor	Wages
Management	Profits

We have noted above reasons for doubting the advisability of giving land a separate place. In an earlier lesson (see page 32), the question is raised whether there are not innumerable factors in production. The latter point is thus put by Davenport:

"The employer's computation of costs includes items other than wages of labor, rents of instruments, interest on the value

> fund invested, and his own necessary profits. Other costs, as for example, risk burdens, are to be computed; taxes and advertising expenses, deterioration charges, subscriptions made on grounds of business expediency—tickets to the church supper, contributions to the Sunday school picnic, copies of the *War Cry* accepted—must all be included; the purchase of machinery or a franchise or a patent or a state legislature may be undertaken for equally cogent business reasons."

It is, however, quite possible to include all of these various outlays and corresponding incomes, under a few heads. The typical employer or entrepreneur, producing goods for the market, finds that his requirements whether for manufacturing or for selling can be grouped in the following classes

I. Primary: *Capital,* in the form of unspecialized loan-fund, that is, money or rights or power to purchase goods or services.

II. Secondary, that is, necessary instruments of production, goods or services or privileges, to secure which this capital must be invested.

1. *Privilege* to do business, e.g., taxes paid to a state, payment for a franchise, or for a patent; the banana peddler's payment to a grafting policeman, or the railroad corporation's subscription to a party campaign fund.
2. *Capital goods*, concrete instruments of production, land, buildings, machinery, raw materials, fuel, power, etc.
3. *Labor*, employed under direction, manual and clerical, skilled and unskilled.
4. *Management*, the services of the directing head, whether a single man or several partners or the more complicated control exhibited in the modern corporation.

All of the outlays mentioned in the quotation from Davenport fall under one or other of these heads: depreciation charges are on the same footing as outlay for new plant, that is, are equally investment in capital goods; the *War Cry* subscription falls under advertising, which, again, is to be classified in one or more of the above categories according to the method of publicity adopted,—whether one's own front window is used, or a bill-board or a newspaper column rented, or a sandwich-man hired.

We are, however, primarily concerned with the shares in distribution, not with the outlays in production. We may vary the above classification, therefore, to show who or what are the necessary factors, and what are the shares in distribution which correspond:

Factors in Production	Corresponding Shares in Distribution
Property or Rights:	
Privilege to do business. Capital goods. Capital loan-fund.	*Rent*, where payment is expressed as a definite sum per unit of property. *Interest*, where payment is considered as a fraction of the capitalized value of the property or right.
Services:	
Labor under direction	*Wages.*
Management	*Profit.*

This classification, it will be seen, differs from the older one noted above chiefly in considering rent and interest as related terms, different means of expressing the same share in distribution. It is thus more in conformity with business usage. This point will be discussed further in the next lesson.

Forces Determining the respective Shares in Distribution.

What, then, can we say are the forces or laws determining the shares thus classified? It appears impossible to frame a separate law for each factor, as Ricardo attempted to do in the case of Rent. Distribution is in brief a bargaining process, and the share of each depends vitally on the strength or weakness of the other factors in the bargaining, and cannot be determined apart from the other shares. The share which any factor receives depends upon its power to make good its claim, not upon its actual contribution to the whole product—an amount which cannot be ascertained. The more indispensable any factor can make itself, the larger will be its reward. The most tenable theory of distribution, then, is that which recognizes that relative bargaining strength is the only general principle which can be asserted, and which then proceeds to examine in the case of each factor what are the main sources of strength and weakness in its position. In the lessons which follow this will be done with each factor in turn.

Questions for Review.

1. What are the usually recognized shares in distribution?

2. What instances do you know of where men receive income under more than one of these classifications?

3. Why did economic discussion develop more notably in the United Kingdom than in any other country, during the nineteenth century?

4. Why did Ricardo and his followers lay such stress on agricultural land and its rental?

5. State briefly the Ricardian law of rent. On what principles is it based?

6. What is the margin of cultivation? What wheat is grown under the most unfavorable circumstances? Is rent a factor in the cost of production?

7. If all land were equally desirable, could there be rent? Does rent inevitably exist if lands of different fertility are cultivated?

8. What would be the effect upon rent of the discovery of new land? the building of a railway into a new district?

9. If the state owned all the land would there be any rent?

10. What is the subsistence theory of wages?

11. Did Ricardo recognize the influence of the standard of living?

12. What was the outdoor poor relief system which existed in England in the early years of last century?

13. What is the essential difference between the subsistence and the wage-fund theories?

14. What determined the size of the wage-fund?

15. What determined the number of applicants for a share in it?

16. What was the bearing of the doctrine on trade union agitation?

17. What justification of profits was offered by the classical economists?

18. Is land a separate and distinct factor from "capital"?

19. What were the sound elements in the subsistence and wage-fund theories?

20. What was Walker's theory of wages? Outline the later productivity theories. What use is made of the idea of a margin of production? of the idea of rent as being a surplus?

21. What are the shares in distribution, according to the present-day classification?

22. What is the bargaining theory of distribution?

Questions for Written Answer.

1. What is the Law of Diminishing Returns? Make clear the different senses in which the term is used.

2. Define necessaries, and show how the subsistence theory could be made either an "iron law" or a "golden law" of wages.

3. Take some industrial enterprise known to you, and (1) classify the outlays made and (2) classify the shares into which the total proceeds are divided.

4. Answer any two of the Review questions.

5. Have you any other difficulty?